

## **I. INDIVIDUAL INCOME TAXES**

### **CHAPTER 1**

#### **REDUCE MARGINAL TAX RATES**

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##### **General Explanation**

##### **Chapter 1.01**

##### **Current Law**

The amount of tax imposed on taxable income in excess of the zero bracket amount of individuals varies from a minimum rate of 11 percent to a maximum rate of 50 percent. There are different rate schedules for four classes of taxpayers: (1) married individuals filing jointly and certain surviving spouses (14 tax rates); (2) heads of households (14 tax rates); (3) single individuals (15 tax rates); and (4) married individuals filing separately (14 tax rates). The progression of the rates for each class of taxpayers is adjusted annually for inflation as measured by the Consumer Price Index for all-urban consumers (CPIU).

##### **Reasons for Change**

The accumulation of tax exclusions and deductions over the years has substantially eroded the tax base, forcing higher rates of tax on income that is subject to tax. High marginal tax rates create disincentives for saving, investing, and working. These in turn constrict economic growth and productivity.

The Administration proposals would expand the base of income by eliminating many current deductions and exclusions unrelated to the proper measurement of taxable income. This expanded base permits a significant reduction in marginal tax rates without impairing Federal income tax revenues.

##### **Proposal**

The current 14 tax rates (15 for single taxpayers) would be replaced by three rates -- 15, 25, and 35 percent as shown on Table 1. The applicable tax rate brackets would be indexed as under current law.

### Effective Date

The proposed individual tax rates would be effective July 1, 1986. Thus, the rate schedule for taxable years beginning on or after January 1, 1986, would reflect blended rates based on the new rates effective on July 1. Withholding to reflect the rate reduction would change on July 1, 1986.

### Analysis

The proposal would reduce individual tax liabilities an average of 7 percent; marginal tax rates on economic income would be approximately 19 percent lower than under current law. The percentage reduction in taxes is greater at the bottom of the income scale than for middle-income families, due to the increase in the tax threshold. Tax liabilities of families with incomes below \$10,000 would fall by an average of 35.5 percent, and the reduction in taxes for families with incomes below \$20,000 would be 18.3 percent.

Table 1.01-1

## 1986 Current Law Tax Rate Schedules

Single Returns		Head of Household Returns		Joint Returns	
Taxable Income	Marginal Tax Rate (percent)	Taxable Income	Marginal Tax Rate (percent)	Taxable Income	Marginal Tax Rate (percent)
Less than \$ 2,480	0	Less than \$ 2,480	0	Less than \$ 3,670	0
2,480 - 3,670	11	2,480 - 4,750	11	3,670 - 5,930	11
3,670 - 4,750	12	4,750 - 7,010	12	5,930 - 8,200	12
4,750 - 7,010	14	7,010 - 9,390	14	8,200 - 12,840	14
7,010 - 9,170	15	9,390 - 12,730	17	12,840 - 17,260	16
9,170 - 11,650	16	12,730 - 16,180	18	17,260 - 21,800	18
11,650 - 13,920	18	16,180 - 19,640	20	21,800 - 26,540	22
13,920 - 16,180	20	19,640 - 25,360	24	26,540 - 32,260	25
16,180 - 19,640	23	25,360 - 31,070	28	32,260 - 37,920	28
19,640 - 25,360	26	31,070 - 36,790	32	37,920 - 49,420	33
25,360 - 31,070	30	36,790 - 48,230	35	49,420 - 64,740	38
31,070 - 36,790	34	48,230 - 65,390	42	64,740 - 92,360	42
36,790 - 44,780	38	65,390 - 88,260	45	92,360 - 118,040	45
44,780 - 59,670	42	88,260 - 116,850	48	118,040 - 175,230	49
59,670 - 88,260	48	116,850 or more	50	175,230 or more	50
88,260 or more	50				

## 1986 Proposed Tax Rate Schedules

Single Returns		Head of Household Returns		Joint Returns	
Taxable Income	Marginal Tax Rate (percent)	Taxable Income	Marginal Tax Rate (percent)	Taxable Income	Marginal Tax Rate (percent)
Less than \$ 2,900	0	Less than \$ 3,600	0	Less than \$ 4,000	0
2,900 to 18,000	15	3,600 to 23,000	15	4,000 to 29,000	15
18,000 to 42,000	25	23,000 to 52,000	25	29,000 to 70,000	25
42,000 or more	35	52,000 or more	35	70,000 or more	35